Monthly Letter

April 2022

prodigy INVESTMENT MANAGEMENT

Invest well. Celebrate life.

We were +5.0% in March vs +4.0% for the NIFTY50. For the financial year ended March 2022, we were +35.3% vs + 18.9% for the NIFTY50 (since inception from 1st March 2012, we were +24.6% CAGR, post fees vs 12.3% CAGR for the NIFTY50, as per the SEBI mandated TWRR method). Markets recovered towards the end of March, as the Russian onslaught seemed to ebb. There is a high probability that markets have seen their worst, however, even if there was to be a ceasefire, we believe that the severe headwinds of elevated commodity prices, arising from sanctions and disrupted supply chains coupled with the monetary tightening by the US Federal Reserve, are likely to result in a muted year for equities in India. Given that the last two years have been super normal years for equity investors, resulting in stretched valuations, the extant inflationary environment we are experiencing, tilts the balance towards a cautious outlook.

The story of the year is arguably the resilience of the Indian markets in the face of heavy selling by FPIs in equities over the last six months (net sales of approximately Rs.1.5 trillion, and in March 2022 alone, a net selling of Rs. 41,000 crores), this is something that augurs well for our market going forward. The outflow in fiscal year 2022 is almost three times the twelve-month rolling outflow for the period ended April 2020, when we experienced one of the worst crashes, with the NIFTY50 falling well over 30% from its peak in January 2020. Never would we have imagined a few years ago, that our market would hold out this well in the face of such selling. We are almost back to lifetime highs notwithstanding this outflow. The surge in domestic participation with the spread of the equity culture, especially amongst younger investors, is a tremendous development over the last couple of years, aided by the proliferation of online brokerages and growing mutual fund participation. Equity holdings as a percentage of the overall domestic savings basket is still low, and this would suggest that this trend still has a lot of headroom left to run.

While domestic demand continues to stay robust, notwithstanding the third covid wave; the severe rise in commodity prices is likely to impact business margins, as beyond a point, such a sharp escalation cannot be passed on. We witnessed a fair amount of this in the Q3FY22 the earnings season and we believe that this is what is likely to reappear in an even more severe form in the Q4FY22 earnings season starting now. While the market is not unaware of this factor, it is possible that the market believes this severe inflation is transitory and has chosen to look beyond this patch. Indeed, with the renewed lockdowns in China and the withdrawal of Russian forces from around Kyiv, commodity prices have started to ease up. However, we remain somewhat circumspect given that earnings growth is what drives valuations, and this under will be pressure.

While we believe this year could be a positive one, the positive domestic growth story is likely to be offset by a weak global impulse. The yield curve in the US is flattening and inverting, something which has been a reliable harbinger of recessions in the past. De-globalisation and protectionism now appear to be entrenched forces, which are likely to impact global trade and investment flows. While India may be on the positive side of some of these forces, on the whole, global growth is likely to be affected, which is not good for any country in the long term. We continue to believe that India is amongst the best placed to grow for the next many years, but markets may not reflect this growth in the near or medium-term in an inflationary environment.

Our challenge now is to find businesses that will be the least impacted by these headwinds or those that can navigate this difficult period best. Travel and entertainment-related businesses that will benefit from the relaxation of covid induced restrictions are likely to do well after two years of pain. Many businesses that are benefiting from disruptive trends should continue to do well. Commodity producers should also benefit (though this area is not our forte and we may not expose ourselves to it given the inherent volatility of commodity price). Thus, there is opportunity and we will do our best to position portfolios to benefit from the same.

Best wishes,

RC

301-302, Mittal Avenue, Kala Ghoda, Fort, Mumbai – 400 001. India Tel: +91 22 22875801